

EXAMINATION QUESTIONS

for

Certified Public Accountants

BULLETIN 622

1947

Commonwealth of Pennsylvania
DEPARTMENT OF PUBLIC INSTRUCTION
Harrisburg



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Commonwealth of Pennsylvania
DEPARTMENT OF PUBLIC INSTRUCTION
Bureau of Professional Licensing
Harrisburg

The State Board of Examiners of Public Accountants
Pennsylvania State Board Examination Questions
December, 1947

EXAMINATION IN GENERAL ACCOUNTING

Monday, December 1, 1947, from 9 A. M. to 1 P. M.

NOTE TO CANDIDATES—Mere answers to questions do not provide sufficient evidence of ability. An appearance of professional workmanship is desired—including neatness, absence of amateur performance, set-up of answers, and clearness of explanations. Place your candidate number and page number at the top right-hand corner. Papers are to be clipped at the top left-hand corner. Hand in paper for each session regardless of whether you answered the questions or not.

QUESTION NO. 1

1. In the examination of the collateral of a bank you find certain loans collateralized by "field warehouse receipts" and other loans collateralized by "public warehouse receipts." Distinguish between the two types of collateral held.

2. What are the objectives of the audit procedures applicable to fixed assets and depreciation reserves?

3. Where management uses standard costs for accounting purposes, what is the effect on the general rule for pricing inventories, namely "cost or market, whichever is lower"?

4. Under Pennsylvania law, from which of the following surplus accounts may dividends be paid?

- a. Earned Surplus
- b. Donated Surplus
- c. Surplus arising from the revaluation of fixed assets by appraisal
- d. Paid in Surplus
- e. Surplus arising at the time of acquisition of subsidiary

5. State two methods of stating the asset "Returnable Containers" on the Balance Sheet of a Company.

6. What are "Intangible Drilling Costs"?

7. Outline the attitude of current accounting authorities in regard to "Reserve for Contingencies," created out of income.

8. What information should be requested from a life insurance company on a confirmation of a policy held on the life of an officer under which the Company is beneficiary?

QUESTION NO. 2

The John Doe Company, incorporated in Pennsylvania, having its plant and principal office in Pittsburgh and reporting on the basis of the calendar year, maintains branch sales offices in New York and Chicago. It owns 51 per cent of the voting stock of the Richard Roe Company, a foreign corporation which does not do business in Pennsylvania. Other relevant facts with respect to the assets of the John Doe Company are as follows:

Assets and Tangible Assets at Actual Values

Total assets at end of the year	\$1,500,000
Total tangible assets at that date	770,000
Tangibles at branch offices at that date	110,000
Year's average of total tangible assets	800,000
Year's average of tangible assets at branch sales offices	115,000

Investments (Held throughout the Year)

Stock of a Pennsylvania business corporation	\$10,000
Stock of the Richard Roe Company	100,000
Five per cent of the stock of a foreign corporation having a plant in Pennsylvania	25,000
United States securities issued after March 1, 1941....	150,000
Bonds of the Richard Roe Company	50,000
Stock of a New York national bank	15,000
Bonds of the City of San Francisco	10,000

Salaries, Wages, Etc., Paid to Employees

Total compensation of employees was \$300,000, of which \$40,000 was earned by managers, salesmen, and others chiefly connected with the branch sales offices. The vice-president also acted as general sales manager and spent 30 per cent of his time at the branch offices. His salary was \$10,000.

Gross Receipts

The items of gross receipts were:

Sales, \$1,000,000; interest, \$3,200; dividends, \$12,000; patent royalties, \$3,500, of which \$2,000 was received from licensees operating in other states and \$1,500 was received from licensees operating in Pennsylvania; sale of scrap at plant, \$1,000. Sales of \$400,000 (included in the total of \$1,000,000) were made by employees chiefly connected with the branch sales offices.

Indebtedness

Throughout the year, blocks of the Company's bonds on which interest was paid were held respectively by (a) individual residents of Pennsylvania, (b) domestic corporations organized for profit, (c) labor union relief associations, and (d) non-resident individuals; and also by (e) Pennsylvania banks or trust companies respectively—

- (1) in their own right
- (2) as trustees for resident individuals
- (3) as trustees for institutions of purely public charity
- (4) as trustees for nonresidents, in general; and

- (5) as trustees for the benefit of nonresidents, where the property or the money for its purchase was originally received from non-resident settlers.

REQUIRED:

1. (a) List the John Doe Company's asset items which are exempt from the capital stock tax. (b) Show the fraction to be used in determination of that part of the value of the entire capital stock which is taxable.
2. (a) If a security exempt from capital stock tax had been held at the beginning of the year but not at its close, would any exemption on account thereof have been allowable? (b) If so, how would the allowance have been computed?
3. If after the beginning of the year the Company had bought an exempt security and had sold it before the year's close (so that it does not appear on the balance sheet of the capital stock tax report for the taxable year and did not appear on the balance sheet of the report for the previous year), would the Company have been entitled to allowance therefor?
4. Show the respective fractions for allocation, for corporate net income tax purposes, of the Company's (a) tangible assets, (b) compensation of employees, and (c) gross receipts.
5. Which holdings of the Company's bonds are subject to the tax on corporate loans?
6. If, although performing his official duties in Pittsburgh, the Company's treasurer had resided with his family in Youngstown, Ohio, could Pennsylvania have required him to withhold the corporate loans tax?
7. An individual resident of Pennsylvania held some of the Company's bonds throughout 1944, 1945, and 1946. No interest was paid in 1944 or 1945. In 1946 the Company paid the back interest and also paid interest in full for 1946. Should the treasurer have withheld tax for 1944 and 1945 as well as for 1946?

QUESTION NO. 3

The opening trial balance of the Borough of Wm. Penn as of January 1, 1946, was as follows:

	<i>Dr.</i>	<i>Cr.</i>
Cash	\$50,000.00	
Taxes Receivable	30,000.00	
Tax Liens	10,000.00	
Miscellaneous Accounts Receivable	2,000.00	
Audited Claims Payable		\$60,000.00
Warrants Payable		10,000.00
Reserve for Contracts and Open Market Orders.....		8,000.00
Surplus		14,000.00
	\$92,000.00	\$92,000.00

PENNSYLVANIA DEPARTMENT OF PUBLIC INSTRUCTION

The following transactions occurred during the year 1946:

The budget adopted for the year 1946 provided for appropriations of \$500,000.00, estimated tax revenues of \$450,000.00, and estimated miscellaneous revenues of \$50,000.00.

Taxes assessed aggregated \$460,000.00.

Bills rendered for miscellaneous revenues amounted to \$48,000.00.

Cash receipts were as follows:

Taxes—Current Year	425,000.00
Taxes—Prior Year	25,000.00
Tax Liens	10,000.00
Miscellaneous Accounts Receivable	45,000.00

Cash of \$500,000.00 was paid in settlement of warrants payable.

Contracts and open market orders placed, and payrolls, all chargeable against the current year's appropriations amounted to \$495,000.00.

Claims filed and approved for contracts, open market orders, and payrolls applicable to the current year amounted to \$450,000.00.

Warrants drawn in payment of current year's claims amounted to \$445,000.00.

Claims were filed and approved and warrants were drawn for previous year's commitments on contracts and open market orders.

Warrants were drawn for all audited claims payable at January 1, 1946.

Note: All figures included above are not of discounts.

Unpaid taxes for years prior to 1946 were all liened during 1946.

REQUIRED:

1. Prepare journal entries to record the above transactions and to close out the nominal accounts. Balances in appropriation accounts and in estimated revenue accounts lapse at the close of the year.
2. Prepare a balance sheet as of December 31, 1946.

QUESTION NO. 4

BALANCE SHEETS, DECEMBER 31, 1946

ASSETS

	Company A	Company B
Cash	\$ 100,000	\$ 50,000
Accounts Receivable, Trade	200,000	100,000
Accounts Receivable, Company B	100,000	—
Inventories	300,000	150,000
Investment in Company B	150,000	—
Fixed Assets, Net of Depreciation Reserves.....	275,000	45,000
Deferred Charges	25,000	5,000
	<u>\$1,150,000</u>	<u>\$350,000</u>

CERTIFIED PUBLIC ACCOUNTANTS EXAMINATION—1947

LIABILITIES

Accounts Payable, Trade	\$ 125,000	\$ 35,000
Accounts Payable, Company A	—	90,000
Accrued Taxes	100,000	30,000
Accrued Payroll	25,000	5,000
	<u>\$ 250,000</u>	<u>\$ 160,000</u>

CAPITAL STOCK AND SURPLUS

Capital Stock	500,000	100,000
Capital Surplus (Paid in)	100,000	25,000
Earned Surplus	300,000	65,000
	<u>\$1,150,000</u>	<u>\$ 350,000</u>

STATEMENTS OF PROFIT AND LOSS

For the Year ended December 31, 1946

	Company A	Company B
Sales—To Company B	\$ 600,000	\$
Sales—to Others	600,000	850,000
	<u>\$1,200,000</u>	<u>\$ 850,000</u>
Cost of Sales—To Company B	\$ 450,000	\$
Cost of Sales—To Others	400,000	650,000
	<u>\$ 850,000</u>	<u>\$ 650,000</u>
Gross Profit	\$ 350,000	\$ 200,000
Selling and Administrative Expenses	159,000	125,000
	<u>\$ 191,000</u>	<u>\$ 75,000</u>
Add, Dividend Received, Company B	9,000	—
	<u>\$ 200,000</u>	<u>\$ 75,000</u>
Provision for Income Tax	75,000	25,000
Net Profit	<u>\$ 125,000</u>	<u>\$ 50,000</u>

ANALYSES OF SURPLUS

For the Year Ended December 31, 1946

	Company A	Company B
Earned Surplus, Balance, January 1, 1946	\$ 250,000	\$ 25,000
Add, Net Profit for Year	125,000	50,000
	<u>375,000</u>	<u>75,000</u>
Less, Dividends Paid	75,000	10,000
Earned Surplus, Balance, December 31, 1946	<u>\$ 300,000</u>	<u>\$ 65,000</u>
Capital Surplus, Balance, January 1 and December 31, 1946	<u>\$ 100,000</u>	<u>\$ 25,000</u>

The following additional information is ascertained in connection with the assignment.

1. Ninety per cent of the outstanding capital stock of Company B was acquired by Company A on January 1, 1946.

2. Company B did not handle products of Company A until about January 15, 1946. All sales of Company A to Company B were on a fixed mark-up which did not change during year. During 1946, Company B disposed of the Inventory on hand at December 31, 1945 and became a distributor of the products of Company A only.

3. On December 31, 1946, \$10,000 of merchandise was shipped to Company B, F.O.B. plant of Company A, and such merchandise was received by Company B on January 3, 1947.

REQUIRED:

Prepare the consolidated financial statements for the year 1946.

Monday, December 1, 1947, from 2 P. M. to 5 P. M.

QUESTION NO. 5

The Frugal Tool Company's trial balance at December 31, 1946 includes: Repairs, Machinery, and Equipment \$17,300; Advertising \$22,300; Shipping Expense \$17,500; Factory Supplies and Expenses \$5,000; Repairs, Buildings \$1,300; Loss on Damage Suit \$2,500; Heat, Light and Power \$10,100; Inspection Expense \$13,100; Depreciation \$20,000 (Factory portion \$15,600); Branch Office Selling Expense \$38,100; Real Estate Taxes \$3,000 (Factory portion \$2,900); Administrative Clerical Salaries \$14,200; Insurance \$1,300 (Factory portion \$1,000); Social Security Taxes \$5,700; (Factory portion \$4,800); Bad Debts \$4,800; Charges Due to Bad Workmanship \$3,600; Factory Supervision Salaries \$6,600; Management Salaries \$7,000 (Allocable to factory \$5,200); Indirect Factory Wages \$13,500; Interest Received \$2,200.

During 1946, the Company has absorbed Manufacturing Burden at a standard (pre-determined) rate of \$2.00 per productive machine hour.

The Inventory at December 31, 1946 includes no merchandise that was on hand at December 31, 1945. Included in the work in process and finished goods inventories at December 31, 1946 were materials which required 20,000 productive machine hours.

During 1946, the Company put 100,000 productive machine hours in process.

REQUIRED:

What adjustment, if any, would you make to the inventory of the Frugal Company at December 31, 1946? Show your calculations and the adjusting entry (if needed).

QUESTION NO. 6

The Workers' Labor Union has requested you to review its accounting system. Your investigation revealed the following:

The Workers' Labor Union is an industrial union; that is, its members are organized by plants, rather than by crafts.

It has 1,000 local unions, with a total membership of 250,000. The territory covered is divided into 25 geographical districts to which the local unions are assigned according to location.

The executive and administrative functions are conducted from the Central Office, which comprises the following departments: Accounting, Research, Publicity, Local Unions, and Legal. In addition, the officers and certain employees perform general duties and are not assigned to any specific departments.

Each district has a District Office, supervised by a District Director. The District Offices handle ordinary local union problems, organizing activities, and minor industrial disputes, and are staffed by office personnel and assistants to the District Directors.

All accounting records are maintained at the Central Office. All expenditures, except for minor items paid by District Offices out of petty cash funds are made from the Central Office. Checks are signed by the treasurer and one other officer. Petty cash funds at the District Offices are imprest funds and are reimbursed monthly by the Central Office for expenditures as reported by the District Directors. Data supporting the expenditures are retained by the District Offices.

Revenues of the union consist of initiation fees and dues of members and miscellaneous income, which are recorded on the cash basis rather than on the accrual method. Members who work less than ten days during a month are exonerated from payment of dues for that month.

Initiation fees are collected by the Financial Secretaries of the local unions and remitted to the Central Office, together with reports showing the number of members at the beginning of the month, changes during the month, the number of members at the end of the month, and the number of members entitled to refunds because of insufficient work time. These reports are filed in the order in which they are received.

All collective bargaining contracts contain the "check-off" clause under which the employer deducts the union dues from the payroll and remits to the Central Office.

One-half of the initiation fees and one-half of the dues are retained by the Central Office, the other half being refunded to the local unions. Exonerated dues collected are also refunded to the local unions for return to the proper members.

Funds of local unions are not part of the assets of the Central Office. Each local union keeps its own records and its officers are primarily responsible to the members. Records pertaining to initiation fees, dues, and refunds, including refunds of exonerated dues, are audited by representatives of the Central Office.

Central Office expenses which are recorded on the accrual basis, are distributed to the following accounts in the general ledger:

Rent, Light, and Heat	Travel Expense
Office Supplies and Expense	Printing
Telephone and Telegraph	Conferences
Salaries	Organizing Expense

PENNSYLVANIA DEPARTMENT OF PUBLIC INSTRUCTION

District Office expenses are similar to those of the Central Office but all are charged to one account in the general ledger entitled "District Office Expense." No separate record is kept of the details of this account.

A description of the principal accounting records maintained in the Central Office follows:

1. Cash Receipts Register—columns headed as follows:

Date
From whom received
Net cash (debit)
Miscellaneous income (credit)
General ledger — separate columns for account and amount (credits in black—debits in red)

Entries are made by employe A, who also keeps the General Journal and General Ledger.

Receipts of initiation fees and dues are recorded in the Income Register, described later.

2. Cash Disbursements Register—columns headed as follows:

Date
Check number
Payee
Amount of check (credit)
Discount (credit)
Accounts payable (debit)

Entries are made by employe B. Each day's checks are arranged alphabetically, before numbering, in order to facilitate finding checks when only payee's name is known. Checks for per capita refunds of initiation fees and dues are entered in a separate record.

3. Per Capita Refund Check Register—columns headed as follows:

Date
Check number
Local Union number
Amount of check (credit)
Initiation fees refund (debit)
Dues refund (debit)

Entries are made by employe B, who makes up checks every two or three weeks.

4. Income Register—columns headed as follows:

Date
Local Union number
Total amount received (debit)
Initiation fees (credit)
Dues (credit)

Entries are made by employe C, who also makes deposits.
Miscellaneous income is recorded in the Cash Receipts Book.

5. Voucher Register—columns headed as follows :

Date
Payee
Voucher number
Accounts payable
District Office expense
Central Office expense—separate columns for account
and amount
Miscellaneous — separate columns for account and
amount

Entries are made by employe D, who also approves vouchers for payment.

Vouchers are filed numerically, but are arranged alphabetically before numbering. Refunds to Local Unions for members who were exonerated from payment of dues because of insufficient work time are recorded in this register.

6. Pay Roll Record—columns headed as follows :

Name
Gross earnings.
Travel expense
F.O.A.B.
Income tax
Bonds
Other deductions
Net pay
Check number

When away from home, employes are paid per diem expenses of \$10.00 on the basis of reports showing only the number of days the employe was away from home. Per diem expenses are added to pay checks. Total of net pay column is entered as one amount in the Cash Disbursement Record, with beginning and ending check numbers shown; distribution to accounts of totals of columns is made by journal entry. This summary and individual employe records are kept by employe E, who also files all payroll tax returns when due, and prepares forms W-2 at the end of the year. Individual employe records which are kept in a Kardex File, show the name, address, and Social Security number of the employe and contain the following columns :

Date
Gross pay
F.O.A.B.
Income tax
Bonds
Other deductions
Net pay

The General Ledger and General Journal are ruled in the usual manner.

REQUIRED:

Make specific recommendations as to changes and additions to existing records with the view of:

- (a) Effecting better internal control, and
- (b) Improving the records and recording procedures at the Central Office. In this connection, it is desired that salaries and travel expenses of the Central Office be shown by departments and the District Office expenses be broken down into the classifications mentioned.

It is also desired that a record be maintained of initiation fees, dues, and per capita refunds, showing the amounts applicable to each local union.

QUESTION 7

You are engaged by the X Bus Company (operating under the Inter-State Commerce Commission classification of accounts) to make an examination of the company's financial statements at the end of the current fiscal year, prepare the Federal income tax return, and advise the accounting official of the company with reference to an accounting and related tax problems that may arise before the end of the year. The following questions are presented to you and an answer by letter is requested:

1. Does the company, which uses the unit plan of depreciation, have any option as to the method of computing depreciation of buses? If so, discuss the method permitted.
2. Additional buses are required and it is necessary to finance the purchase thereof. Should the interest charges relating thereto be treated in a manner similar to interest during construction, or be charged to expense? Are such charges deductible in computing the Federal income tax of the company?
3. The company charges 10c per ride, but also sells books of fifty tickets (good for three months) for \$4.50, whereby the rider saves 50c (or 1c per ride). As many tickets are in the hands of the public at the end of any fiscal period, how should the sale and collection of such tickets be accounted for on the general books? How should the proceeds from sales of these tickets be considered in estimating the Federal income tax to be accrued?

4. The client has under consideration several transactions relating to a prior period which have not as yet been recorded on the books. What is your suggestion in general as to the recording thereof?

REQUIRED:

Prepare your letter of reply, giving due consideration to the various phases of the engagement with which you are concerned.

Tuesday, December 2, 1947, from 9 A. M. to 2 P. M.

QUESTION NO. 8

Four Theory Questions

1. FACTS:

On September 30, 1946, Jones Corporation purchased from its president a property used for manufacturing operations and, in payment thereof, issued 20,000 shares of its capital stock having an aggregate par value of \$2,000,000. In the accounts of Jones Corporation, an amount of \$2,000,000 was debited to property account and a like amount was credited to capital stock account.

On October 10, 1946, the president, pursuant to a previous understanding, donated 5,000 of the above shares to the Jones Corporation and on October 15, 1946, all of the donated shares were sold for cash at par value. At the direction of the president, the proceeds of the sale were credited to earned surplus of the corporation. The comptroller of the corporation is of the opinion that the credit should have been made to capital surplus. You are thereupon called in to advise the president and the comptroller as to the proper accounting treatment.

REQUIRED:

How would you advise the president and the comptroller to record the above transactions?

2. FACTS:

During the year 1946, Jones Company reacquired 1,000 of its 10,000 issued shares of capital stock. One-half of the reacquired shares was placed in a special fund for replacement of equipment and the other half was earmarked as treasury stock. On December 30, 1946, Jones Company paid a dividend of \$50,000 (\$5.00 per share) and disposed of the dividends on reacquired shares as follows:

Amount added to special fund cash for replacement of equipment and to reserve for replacement of equipment	\$2,500
Amount added to general cash and to income from dividends	\$2,500

REQUIRED:

If you disagree with the above allocation and treatment, what treatment would you advise?

3. FACTS:

During 1940, James Company, which owned and operated a number of enterprises, purchased the assets and business of Prosperity, Incorporated, and paid therefor \$10,000,000 in cash. The assets of Prosperity

Incorporated, were represented by its manufacturing plant and by a patent to manufacture its product. The exclusive privilege to manufacture will expire in ten years from January 1, 1941.

It was determined by the James Company that the tangible assets purchased had a value of \$5,000,000 and such amount was debited to the appropriate asset account. The other \$5,000,000 was assigned as the cost of the patent to manufacture the product.

James Company, during the five years following the aforesaid purchase, realized an annual return of about 14% on its investment in all of its enterprises and reported annual income of approximately \$4,000,000.

Beginning in 1941 and continuing through 1945, James Company, by annual charges of \$500,000 against earned surplus, wrote down the amount established for the Prosperity, Incorporated, patent from \$5,000,000 to \$2,500,000. During 1946, James Company reduced its capital by \$2,500,000 and concurrently, by charge against the capital surplus so created, wrote off the balance of \$2,500,000 in the patent account.

REQUIRED:

What, if any, would be your exceptions to the above accounting for the disposition of the cost of the Prosperity, Incorporated, patent if you had been called upon to report on the financial statements of James Company for the years 1945 and 1946?

4. FACTS:

Morton Company maintains its principal office in Philadelphia and has branch offices in fifty cities scattered throughout the United States. Most of its liabilities and about ninety per cent of its sales originate at the branches, the accounts of which are examined by a well organized and efficient internal auditing staff. The assets of Morton Company at December 31, 1946, are represented approximately as follows:

	<i>Per Cent</i>
Current assets:	
Receivables:	
Maintained at principal office	1
Maintained at branch offices	6
Inventories:	
Located at principal office	10
Located at branch offices	17
Working funds at branch offices	1
Cash and other current assets at principal office.....	15
Total current assets	50
Fixed assets, investments, and other assets—Accounts maintained at principal office	50
Total assets	<u>100</u>

Morton Company is well managed, its accounts are conservatively stated and from a review of the internal audit reports and procedures of branch operations it appears that there is no reason to question the completeness and accuracy of the work of the internal auditors.

The president of Morton Company has authorized you to make an examination of the accounts of the principal office, review the branch office reports prepared by the internal auditors, and to report on the financial statements of Morton Company for the year 1946.

REQUIRED:

1. On the basis of such examination, would you give an unqualified opinion, a qualified opinion, or no opinion?
2. State your reasons in support of your answer to No. 1.

QUESTION NO. 9

You have been asked by the management of the Blank Manufacturing Company to determine the "break-even point" on a monthly basis, that is, the amount in dollars of sales volume necessary each month to absorb fixed expenses. In other words, you are asked to determine the amount of sales which will result in no gain or loss, but below which a loss will result and above which a gain will result.

Your investigations have resulted in the following statement as the best information available at the time. For convenience in making your computations, the fixed expenses have been segregated from the variable expenses, as indicated. The statement is for a 6-month period.

BLANK MANUFACTURING COMPANY

STATEMENT OF PROFIT AND LOSS

January 1 to June 30, 1947

Gross Sales, less allowances, etc.	\$2,450,000
Cost of Sales:	
Inventory, beginning (at cost)	\$400,000
Cost of Manufacture:	
Direct Labor	\$895,000
Direct Material	745,800
Indirect Expense, Variable	238,700
Indirect Expense, Fixed	358,000
TOTAL COST OF MANUFACTURE	2,237,500
	<u>2,637,500</u>
Less: Inventory, ending (at cost)	800,000
TOTAL COST OF SALES	1,837,500
GROSS PROFIT	612,500
Selling and Administrative Expense	
Variable	100,000
Fixed	200,000
	<u>300,000</u>
PROFIT BEFORE INCOME TAXES	312,500
Provision for Federal and State Income Taxes..	126,200
NET PROFIT FOR THE PERIOD	<u>186,300</u>

Your investigations and inquiries have assured you that for the purpose of your computation you may assume the following:

1. That the data you have assembled, including the profit and loss statement are fairly representative of a balanced operation in that there have been no protracted interruptions and there have been no extraordinary profits or losses.

2. That the beginning inventory was stated at costs comparable with costs attained during the 6-month period for which you have obtained a statement.

3. That you need not make any adjustments for possible future changes in sales prices or costs of labor, material, and other expenses.

4. That for the purpose of determining the sales value of goods manufactured (to compare with the manufacturing cost thereof), the same percentage of gross profit will be realized on the ending inventory as was realized on the sales for the 6-month period.

REQUIRED:

1. Statement and computations, showing how you would arrive at the "break-even point," that is, the volume of sales in dollars it would be necessary to attain each month in order to absorb the fixed expenses. This volume would result in no gain or loss; to fall below it would result in a loss, to go above it should result in a gain. Your computations are to be based upon the foregoing statement and the assumptions as stated.

2. Computation showing mathematical proof of the "break-even" volume of sales you have determined.

QUESTION NO. 10

Your client, John J. Brown, Jr., informs you that under the will of his father a trust of approximately \$200,000 was created in which he is trustee and life-tenant, and his daughter, Anna M. Brown, is remainderman.

He lends you copies of the decedent's will, the executors' first and final account, the schedule of distribution and the adjudication. Before putting the information in final form, he suggests that you lay it out roughly on your work-paper for discussion with him.

You have previously installed a simple system for his personal accounts, which he has operated satisfactorily.

Your review of the documents shows the decedent died January 17, 1946, and distribution was as of March 31, 1947, at which date the investments had been reappraised. It also shows the trust consists of U. S. Treasury bonds (fully taxable), municipal bonds, public utility bonds and stocks, industrial stocks, mortgages on a monthly installment basis, and cash. All income to May 31, 1947, was distributed to the life-tenant by the executors.

REQUIRED:

1. Draft the layout of a simple cash book, journal and ledger, outline the opening entry or entries (state whether inventory, cost or reap-

CERTIFIED PUBLIC ACCOUNTANTS EXAMINATION—1947

praised values are to be used) and submit sample entries for the transactions which follow.

2. Submit comments as to what difference there will be between his accounts and the Federal fiduciary income tax returns he must file.

TRANSACTIONS

Dividends received:

1947			
June 10	On 100 shs. General Motors com.	\$ 75.00	
		Interest on bonds:	
July 1	On \$10,000 City of Phila. 4s, due 11-1-66 (These bonds had been included in the inventory at Jan. 17, 1946, at 129, and reappraised at 127½)	200.00	
Oct. 1	On \$10,000 American Tel. & Tel. 2¾, 1961 (Purchased June 26, 1946, for \$11,142.50, reappraised at \$113).....	137.50	
		Installment on mortgage:	
Aug. 1	\$5,000 mortgage previously reduced to \$4,537.50; interest 4%. Monthly installment (principal and interest)..	40.00	
		Sales of investments:	
June 19	100 shs. American Power & Light \$6 pfd. (Purchased Jan. 31, 1947, for \$9,912.50, reappraised May 31, 1947, at 101)	10,172.00	
June 25	\$6,000 Phila. Elec. Co. 2¾, 1974 (Inventory value \$6,036.00, reappraised value \$6,030.00)	6,024.00	
		Stock dividend, common on common:	
July 15	10 shs. Webster Concrete Co. com. received on 100 shs. common. (Inventory value \$11,000 reappraised value \$10,500). In opinion of counsel it is nontaxable.		
Aug. 25	Stock dividend sold for	1,000.00	

Dividend paid in stock of another company:

1947			
June 16	2 shs. Atlantic City Electric Co. received on 100 shs. American Gas & Electric Co. (Inventory value of 100 shs. American Gas & Electric \$4,500. Reappraised at 41½). Quotations for American Gas & Elec. ex-divd. May 9, 1947, 39¼—39. Quotations for Atlantic City Electric May 9, 1947, 19¼—20. In opinion of counsel it is nontaxable.		
Sept. 22	2 shs. Atlantic City Electric Co. sold for.....	42.00	
		Expenses paid:	
June 30	E. C. Wright Co., stationery	10.00	
The above entries need not be posted to the ledger.			

If any of these items would not be classified the same in the Trustee's account as in the Executors' account, please note so that Mr. Brown will not be misled by the Executors' account.

As to the Federal taxes, note the principal difference between the face of a fiduciary return and an individual return. Also note, for the items shown, what differences, if any, there will be in the treatment for taxes and in the treatment in the accounts.

QUESTION NO. 11

1. In the calendar year 1946 the audited statements of the Y Company, a Pennsylvania corporation, disclosed a net profit of \$100,000.00 from operations of the year before provision for Federal or State taxes on income.

2. In arriving at the net profit stated the following items of income were included:

Interest on United States Securities	
Savings Bonds and Treasury Bonds	
issued prior to March 1, 1941 (all 3%) (40,000.00)	\$1,200.00
issued after March 1, 1941 (all 2½%) (40,000.00)	1,000.00
Interest on Municipal Bonds	
(acquired on July 1, 1946) (3%) (25,000.00)	375.00
Gain on the sale of a building used in the business (owned for a period of 15 years)	10,000.00
3. Dividends on Stock of Domestic Corporations	1,000.00
4. Expenses included	
Contributions	4,800.00
Interest on a loan of \$80,000.00 at 3½%, of which \$20,000.00 was borrowed July 1, 1946, in order to purchase and carry the Municipal Bonds which, with the U. S. Bonds are pledged as collateral for the loan	2,000.00
Loss on Sale of Investment in Bonds of other corporations (held for 5 months)	5,000.00
Depreciation of Buildings and Equipment	10,000.00
Amortization of Goodwill	5,000.00
Addition to Reserve for Bad Debts	1,000.00

The reserve for bad debts in addition to the above showed charges for write-off of \$950.00 and collections of accounts previously written off of \$150.00. The Company uses the charge-off method for Federal Income Tax purposes.

5. Earned Surplus contains a credit of 5,000.00 representing the excess of the proceeds, (\$15,000.00) received from an insurance company over the depreciated cost (\$10,000.00) of a small building destroyed by fire during the year (owned 5 years). A contract for \$17,000.00 for the replacement of the building has been executed.

Earned Surplus also contains a credit of 2,000.00 which is the offset of a charge to Surplus arising from Revaluation of Depreciable Fixed Assets and is the amount of depreciation provided in 1946 on a previous appreciation in valuation of fixed assets.

6. The examination of all Federal Returns has been completed to and including the year 1945 and the Report of the Internal Revenue Agent which the Company has accepted discloses a net operating loss of \$10,000.00 to be available to the Company in 1946, resulting in a net operating loss deduction of \$7,925.00.

REQUIRED:

A determination of the Federal taxable net income, properly classified, and the Pennsylvania Corporate Net Income before provision for Federal Income or Pennsylvania Corporate Net Income taxes.

Tuesday, December 2, 1947, from 2 P. M. to 5 P. M.

QUESTION NO. 12

Three manufacturing companies, all partnerships, engaged in similar operations and manufacturing and selling similar products, were considering two proposals first, consolidation and incorporation, and second, sale of the combined business to outside interests.

Following are summary balance sheets as of the agreed date of acceptance of either proposal, and earning statements for one year, which it has been agreed are indicative of the relative earning power of each company as presently constituted:

BALANCE SHEETS	Company	Company	Company
ASSETS	A	B	C
Cash and Receivables	\$400,000	\$650,000	\$400,000
Inventories and other assets	100,000	150,000	150,000
Plant and Equipment (at cost less depreciation)	1,500,000	700,000	50,000
TOTAL ASSETS	2,000,000	1,500,000	600,000
LIABILITIES AND NET WORTH			
Liabilities	500,000	500,000	100,000
Net worth	1,500,000	1,000,000	500,000
TOTAL LIABILITIES AND NET WORTH	2,000,000	1,500,000	600,000
ANNUAL EARNINGS STATEMENTS			
Sales	4,500,000	5,000,000	7,500,000
Cost of Sales	2,500,000	3,000,000	5,000,000
GROSS PROFIT	2,000,000	2,000,000	2,500,000
General and Administrative Expenses (includes partners' salaries)	1,500,000	1,250,000	1,050,000
NET PROFIT BEFORE INCOME TAXES	500,000	750,000	1,450,000

The following statements regarding the management, personnel and prospects of the businesses were recognized and accepted as true. It was these conditions that prompted consideration of the proposals.

1. Company A was an old established concern with a fairly well-kept plant and modern equipment of a capacity in excess of the business it had been able to get. This was due mainly to the gradual retirement from active participation in the business of the managing partners and the press of other interests of the other partners. This condition, coupled with lack of experienced management, technical and sales promotion personnel, and no immediate prospects for the development of such personnel, indicated a need for these qualities which the other companies had.

2. Company B was an average, successful company in that it had adequate facilities for its business, sound and careful management, and well-established customer relationships.

3. Company C, on the other hand, was almost the opposite of Company A. It had little in the way of plant and equipment, leasing most of its facilities, but it had a young, aggressive organization and a wealth of technical sales and managerial ability. In their field they were thought of as eventual leaders in the industry, although comparative newcomers.

It was agreed, based on the foregoing financial statements and facts, that the combined companies would constitute a well-rounded company as to physical assets, capital experience, management, and necessary personnel.

PART I

It was agreed tentatively that in the event of acceptance of the proposal to consolidate and incorporate, the following arrangement would be carried out:

1. The management of Company B would continue to manage and operate its present plant, make available its advice, assistance, and techniques, and participate in the over-all management of the corporation.

2. The production orders would be scheduled in the plants of the corporation with due regard to the most economical operation, provided good quality was maintained. Thus uneconomical production of certain items at one plant could be discontinued and the orders scheduled and combined with production in the plant showing most favorable costs.

3. The management of Company C would transfer and combine its operations with those of Company A at the plant of Company A, and would take over the management of the combined operations, including production and sales. This management would also participate in the over-all management of the corporation.

4. Capital stock in the new corporation would be distributed in the ratio of the combined net worth and good will allocation of each company. In view of all the facts presented, it was agreed that in appraising the value of good will, the rate of earnings of Company B, before provision for income taxes, would be considered normal for all companies and that earnings in excess of that rate were to be capitalized at 20%. In determining total capitalization, if earnings of any company do not attain normal, such deficiency shall not result in negative good will or a deduction from net worth, but shall be considered zero.

However, in allocating the proportion of capital stock to each company for distribution among the partners, consideration shall be given to deficiency from normal earnings or negative good will by elimination or equalization.

You are called upon to prepare the computations and formulas upon which final discussions and agreements may be made.

REQUIRED:

1. Computation of good will of the proposed new corporation in accordance with the foregoing.

2. Computation of the total capitalization of the proposed new corporation in accordance with the foregoing.

3. Computation of the proportion of capital stock of the proposed new corporation to be allocated to each company for distribution among the partners.

PART II

Simultaneously, outside persons are interested in acquiring the three businesses in order to operate them for themselves, but only if all companies can be obtained together. The management and principal personnel are to have no continuing employment with the purchasers.

The figures as hereinbefore set forth have been accepted as to valuations and earning power of the companies as presently constituted.

For purposes of further consideration of the proposal, the following has been tentatively agreed upon as to sale price:

1. One part of the sale price shall consist of the combined net worths of the companies
2. The remainder of the sale price shall be an allowance for good will.

The prospective buyer and seller cannot agree upon a value for good will of the combined companies. However, the buyer has offered \$1,000,000.

Provided the sale price can be agreed upon, the partners of the 3 companies have not yet arrived at a basis for agreement as to the relative value of good will of each company to the other and the share of sale price (if agreed upon) each company should receive for distribution.

You are asked to suggest first, a basis or formula as an approach to agreement of the sale price of good will, and second, a formula for a reasonable allocation of the sale price of good will among the companies for distribution among the partners.

REQUIRED:

1. Suggestion of a basis for agreement of value of good will between buyer and seller, together with such comments as will give your reasoning.
2. Suggestion of a formula for a reasonable allocation of the sale price of good will (or if preferred the entire sale price) among the partners.

QUESTION NO.13

Two Theory Questions

I

FACTS:

The published annual report of the Melay Company for the year 1944 included financial statements of the company and consolidated financial statements of the company and its subsidiary companies. Approximately

65% of Melay Company's assets was represented by investments in ten subsidiary companies (more than 50% interest), 30% was invested in other companies (less than 50% interest), and the remainder was represented by current assets.

A note to the consolidated financial statements stated the policy as to inclusion of only those companies of which more than 50% of the voting common stock was held by the parent company. Total consolidated assets at December 31, 1944, consisted of (a) Company A and Company B each 15% and (b) Melay Company plus eight other subsidiary companies, 70%.

During the year 1945, Melay Company sold all of its holdings in Company A at cost. The consolidated financial statements for the year 1945 therefore included the parent company and only nine subsidiaries. The consolidation policy note to the consolidated financial statements was worded the same as in the 1944 published report. No disclosure was made as to the sale of holdings in Company A or as to the omission of that company from the 1945 consolidated financial statements.

During the year 1946, Company B changed its accounting period to a fiscal year to end on July 31, and furnished Melay Company with financial statements for the year ended that date. The consolidated financial statements shown in the 1946 report therefore included the parent company and eight subsidiary companies, and a note thereto explained the circumstances pertaining to the omission of Company B's financial statements.

QUESTION :

1. If you had been called upon to report on the financial statements of Melay Company and the consolidated financial statements of Melay Company and subsidiary companies for the year 1945, would you have (a) qualified your report for the reason that

- (1) the consolidated principal had not been applied on a basis consistent with that of the preceding year.
 - (2) no disclosure had been made as to the sale of holdings in Company A despite the fact that Melay Company sustained neither profit nor loss on such sale,
- or (b) deemed it adequate to insert an explanatory paragraph in your report.

QUESTION :

2. If you had been called upon to report on the aforesaid financial statements for the year 1946 would you have (a) qualified your report for the reason that

- (1) the consolidation principle had not been applied on a basis consistent with that of the preceding year?
 - (2) the consolidated financial statements did not present fairly the consolidated financial condition or consolidated results of operations,
- or (b) given an unqualified report in view of the company's note pertaining to the omission of the financial statements of Company B?

II

FACTS:

Unfortunately, the Smith Company had neither earned, capital, or any other type of surplus at January 1, 1946. It did have a substantial arrearage in dividends on its preferred stock. During the year 1946, the operations of the company resulted in net income of \$100,000. In addition to its ordinary operations, Smith Company had transactions as follows:

January 31, 1946—Purchased certain shares of its common stock at a cost which was \$15,000 less than the aggregate par value and thereupon recorded a profit of \$15,000.

May 31, 1946—Purchased and retired certain of its outstanding bonds at a cost which was \$10,000 greater than the aggregate principal amount of the bonds.

July 31, 1946—Sold the shares of common stock which it purchased on January 31, 1946, for \$10,000 less than the par thereof.

November 30, 1946—Purchased certain shares of its preferred stock at a cost which was \$2,000 less than the aggregate stated value of such shares. The company recorded a profit of \$2,000 on these shares. Accumulated, unaccrued, and unpaid dividends on such shares amount to \$5,000.

December 15, 1946—Sold certain of the shares of preferred stock which it purchased November 30, 1946, at a price which was \$4,000 in excess of cost. Accumulated, unaccrued, and unpaid dividends on the shares sold amounted to \$2,500 and \$2,600 on November 30 and December 15, respectively.

QUESTION:

1. How would you advise Smith Corporation to treat the decrease in dividend arrearage resulting from the transactions in preferred stock?
2. In view of the fact that the net result of the transactions listed in the foregoing appears to be immaterial in relation to the net income from operations, would you advise Smith Corporation to dispose of the net result through income?
3. If you disagree with treatment of disposition through income, how would you advise the Smith Corporation?

QUESTION NO. 14

You are called in, in February, 1949, by the president and principal stockholder of a small manufacturing company. He informs you that an audit had been made for the year 1947 by another accounting firm, and he gives you the balance sheet 12/31/47 and operating statement for 1947, all of which he believes to be correct. Accept them as correct.

He gives you the balance sheet 12/31/48 and the operating statement for 1948, as prepared personally by his treasurer, which shows a satisfactory profit, after provision for income taxes of \$29,341.42. He in-

PENNSYLVANIA DEPARTMENT OF PUBLIC INSTRUCTION

forms you that he personally supervised the taking and pricing of the inventory (which resulted in an adjustment crediting income with \$25,-545.39), (of which \$380.53 applied to raw material and \$25,164.86 to work in process and finished stock) and is satisfied that it is correct.

The president tells you that he is worried because, with such profit, and without any unusual plant expansion, his notes payable and other liabilities are increasing, and cash remains at a low point. He advises you that, as far as he knows, collections are being made currently. He knows that the 1948 sales were about the same as those for 1947, and that selling prices, wage levels, cost of materials, etc., have not varied materially from those of 1947.

He informs you that the payroll record is divided into direct labor, indirect labor, and construction labor, the former being charged to work in process, the indirect labor to manufacturing expense, and the construction labor to the fixed asset account. There were no wages payable at the end of either 1947 or 1948.

He advises you that a job order record of work in process inventory is maintained, the account being charged with materials and labor, plus 40% of direct labor for overhead, the latter being credited to an account called "manufacturing overhead absorbed." Credits to the account are made for the accumulated costs shown on the job orders. Charges to the individual job orders are made from material requisitions and direct labor details. When the large credit inventory adjustment occurred in the work in process account, the president asked for an analysis for the two previous years, and received the following:

	1947	1948
Balance, beginning of year	52,706.58	56,290.15
Direct labor charged to account	123,657.37	109,442.17
40% of above	49,462.95	43,776.87
Material requisitions charged to account	110,921.40	113,460.03
Inventory adjustments	2,072.91	25,164.86
TOTAL	<u>338,821.21</u>	<u>348,134.08</u>
Less: Charges to cost of sales based on accumulated		
costs shown on job orders	282,531.06	287,714.58
Cost of inventories on consignment		7,000.00
TOTAL	<u>282,531.06</u>	<u>294,714.58</u>
 Balance at end of year	 56,290.15	 53,419.50

REQUIRED:

You put down the 1947 and 1948 figures which he has given you on the attached worksheet. The president tells you he feels something is seriously wrong with the 1948 figures presented to him by the treasurer and asks you to review them and indicate the weaknesses, if any. Do not attempt to prove anything is wrong; merely indicate if any discrepancies in the 1948 statement are apparent and what steps should be taken to prove or disprove their accuracy.

CERTIFIED PUBLIC ACCOUNTANTS EXAMINATION—1947

	Balance Sheet Dec. 31, 1947		Statement for 1947		Balance Sheet Dec. 31, 1948		Statement for 1948	
	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.	Dr.	Cr.
Cash	4,628.94				4,862.42			
Investment—6% Bonds	12,000.00				12,000.00			
Notes Receivable	3,000.00							
Accounts Receivable	42,107.61				72,391.50			
Inventory, Raw Material	15,680.12				18,521.40			
Inventory, Work in Process and Finished Stock	56,290.15				53,419.50			
Inventory on Consignment	1,200.00				11,200.00			
Land	7,000.00				7,000.00			
Buildings, Machinery & Equipment... Reserve for Depreciation, Buildings, Machinery and Equipment	99,290.23				129,421.05			
Prepaid Expense Accounts	560.00				560.00			
Note Payable		36,416.02				42,957.22		
Accounts Payable		5,000.00				25,000.00		
Commissions Payable		19,624.98				23,220.53		
Provision for Income Taxes		1,000.00				5,499.92		
Capital Stock		15,920.22				19,560.95		
Surplus		150,000.00				150,000.00		
Sales		13,795.83	410,617.47			43,137.25	417,303.09	
Sales Allowances and Discounts			7,250.49				10,700.57	
Freight Out			6,294.80				6,590.18	
Cost of Sales			282,531.06				284,714.58	
Depreciation on Manufacturing Equipment							6,041.20	
Indirect Labor—Manufacturing			5,210.70				10,420.16	
Other Manufacturing Expense			7,210.60				37,408.16	
Inventory Adjustments			38,475.28					
Manufacturing Overhead Absorbed... Office and Executive Salaries				2,140.00			25,545.39	
Selling Salaries				49,462.95			43,776.87	
Commissions			27,610.94				28,910.04	
Interest—Bank Loans			15,620.14				16,100.17	
Depreciation Office Equipment			24,079.92				27,040.23	
Other Administrative and General Expense			210.00				900.00	
Interest on Bonds			500.00				500.00	
Other Interest and Discount			9,742.17				10,218.40	
Provision for Taxes on Income				720.00				1,820.71
Net Profit carried to Surplus				1,596.24				19,560.95
			15,920.22				29,341.42	
			23,880.34					
	241,757.05	241,757.05	464,536.66	464,536.66	309,375.87	309,375.87	488,446.06	488,446.06

EXAMINATION IN COMMERCIAL LAW

Wednesday, December 3, 1947, from 9 A. M. to 1 P. M.

NOTE TO CANDIDATE—Read carefully each question in full before writing your answer. Do not repeat the question as printed. Where a request is made for an explanation, give the answer first and then state the applicable rules of law.

Each question is entitled to the weight as shown.

QUESTION NO. I — WEIGHT: 10 POINTS

1. Does a seal on a contract import a consideration or dispense with it?
2. Is forbearance to sue sufficient consideration for a contract?
3. Is the promise to do what a man is obligated to do sufficient consideration for a contract?
4. Give two instances where past consideration is sufficient to support an oral promise?
5. Is a written promise to repurchase certain shares of stock enforceable where the contract fixes no price at which the shares are to be repurchased? Explain.
6. Is a written promise by one party (promisor) to buy from another party (promisee) all of a certain kind of material that the promisor may require for the year 1947, at a fixed price per unit, enforceable by the promisee? Explain.
7. Where an offer is made to one person, but a third person, upon learning of the offer, accepts the offer in his own behalf, does such acceptance of the offer bind the offeror? Explain.
8. Is a qualified acceptance of an offer an acceptance which will bind the offeror? Explain.
9. May a minor, who, for a valuable consideration, has executed a release for personal injuries, disaffirm the release before or upon becoming of age? Explain.
10. a. Who may be decreed to be a feme sole trader?
b. Name two rights or privileges of such person.

QUESTION NO. II — WEIGHT: 10 POINTS

1. a. What is a "bill of lading?"
b. Explain the difference between a "straight" and an "order" bill of lading as issued by a common carrier of goods.
c. In what manner is the title to *each* transferred?
2. a. Explain the nature of the liability of a common carrier of goods for loss or injury to merchandise during transit.
b. Name four circumstances which will excuse the carrier of liability.
3. When does the liability of a common carrier of goods begin?
4. a. In the absence of a controlling provision in the bill of lading, when does the liability of a common carrier of goods as such cease?
b. In what capacity does the common carrier thereafter hold the goods?

5. Where a common carrier of goods, due to a mistake, charges the shipper less than the lawful rate as established by the filed tariff, what is the liability of the shipper for the deficiency?

QUESTION NO. III — WEIGHT: 10 POINTS

Amos Budd, as the disclosed agent of Curtis Duff, acting within the apparent scope of his authority, orally ordered from Edmund Fry 100 dozen (pairs) of nylon hose of a standard quality at \$8.00 per dozen F.O.B. Edmund Fry's factory. He gave nothing in earnest to bind the contract or in part payment thereof. Edmund Fry, having the hose in stock, immediately shipped the same to Curtis Duff by common carrier using an order bill of lading. Curtis Duff, before actually receiving the hose, notified Edmund Fry that Amos Budd had exceeded his authority in placing the order. Curtis Duff thereafter refused to accept any of the hose.

- a. Did the title of the hose pass to Curtis Duff at any time? If so, when?
- b. What rights, if any, has Edmund Fry against Amos Budd? Explain.
- c. What rights, if any, has Edmund Fry against Curtis Duff? Explain.
- d. If Amos Budd's authority from Curtis Duff had been in writing, would Edmund Fry's rights against Curtis Duff be different. Explain.
- e. If Curtis Duff had accepted a part of the shipment, would Edmund Fry's rights against Curtis Duff be different? Explain.

QUESTION NO. IV — WEIGHT: 10 POINTS

You have been requested to prepare a statement showing the distribution to be made of certain funds in the hands of Charles Dare and Edward Fair. They are the liquidating partners of a partnership originally composed of Aaron Brown, Charles Dare, and Edward Fair who traded under the registered fictitious name of Wel-Don Co. Upon investigation you find the following facts:

Aaron Brown for many years conducted a profitable business under the fictitious name of Wel-Don Co. On January 1, 1945, a partnership was formed by Aaron Brown, Charles Dare, and Edward Fair. Aaron Brown, by the terms of the partnership agreement, contributed as capital the assets of his business (no liabilities existed) including good will. The partners agreed that the assets had a value of \$40,000.00 of which \$10,000.00 represented the value of good will. Charles Dare and Edward Fair each contributed, as capital, \$20,000.00 in cash. Between January 1, 1945, and July 1, 1947, Aaron Brown with the consent and approval of the partners withdrew \$15,000.00 as remuneration for services to the partnership. On January 1, 1946, Edward Fair, with the consent of Aaron Brown and Charles Dare loaned the partnership \$5,000.00 without interest. On January 1,

1947, Charles Dare, with the consent and approval of the partners, withdrew \$5,000.00 on account of his share of the profits. No other sums were contributed or withdrawn by the partners. On July 1, 1947, Aaron Brown died and Letters Testamentary were granted to City Bank as Executor of his estate.

After Aaron Brown's death, Charles Dare and Edward Fair caused an inventory of the assets of the partnership to be made as of July 1, 1947. On August 30, 1947, the assets were sold in bulk at the inventory value of \$120,000.00. The surviving partners also collected \$1,000.00 as interest which accrued between July 1, 1947, and August 30, 1947, on certain of the assets included in the inventory. The debts due other creditors as of July 1, 1947, totaled \$10,000.00. No claim is made for the cost of liquidating the partnership or for compensation to the liquidating partners. The partnership agreement is silent as to distribution of the profits.

Prepare a detailed statement showing the distribution to be made by the liquidating partners and in foot notes explain your reasons therefor.

QUESTION NO. V — WEIGHT: 10 POINTS

1. For what period of time is a written "stop payment order," given by a depositor to his bank, effective without renewal?
2. Within what period of time, if any, after the death of the maker of a check, is the payee of the check allowed to present the same for payment to the bank upon which it was drawn?
3. For what two purposes should a depositor examine the cancelled checks returned to him by his bank?
4. In the audit of Arthur Bruce, you find that on December 3, 1932, he loaned \$1,000.00 to Calvin DeWitt on a judgment note. By the terms of the note both the principal and interest were payable fifteen years after date. The note did not express the rate of interest. In accordance with the authority contained in the note, a judgment was entered on the note on December 3, 1932. The judgment was revived on the dates and in the amounts as follows:

December 3, 1937.....	\$1,300.00
December 3, 1942.....	\$1,690.00

Calvin DeWitt paid all costs in entering and reviving the judgment. In what amount should you show Calvin DeWitt's indebtedness as of December 3, 1947? Explain.

5. In the audit of Arthur Bruce, you also find that on December 3, 1945, by written agreement, Arthur Bruce loaned \$10,000.00 to Adventurers Inc., a Pennsylvania business corporation. The loan was repayable on demand and was secured by a corporate note pledging certain negotiable securities. The rate of interest fixed by the written agreement was 8% per annum. To date no interest or principal has been paid.
In what amount should you show Adventurers Inc. indebtedness as of December 3, 1947? Explain.

QUESTION NO. VI—WEIGHT: 10 POINTS

1. a. What is a mechanic's lien?
b. How can an owner of real estate about to enter into a contract for a construction of a building thereon guard against the entry of a mechanic's lien (1) by the contractor and (2) by a sub-contractor?
2. From what time does a mechanic's lien date in the case of new construction?
3. If a purchase money mortgage is executed and dated October 1, 1947, but is not recorded until October 25, 1947, from what date will the lien be effective?
4. a. Does the satisfaction of a mortgage, by the holder thereof, discharge the obligation of a bond secured by the mortgage?
b. If not, what further steps should be taken?
5. Define and discuss the terms "separate property" and "community property" as they are used in the Community Property Act of July 7, 1947.

QUESTION NO. VII—WEIGHT: 10 POINTS

In an audit for Alvan Brill, of Harrisburg, you find among his valuable papers a note in the following form:

Harrisburg, Pa., June 1, 1945.

"12,000.00

One year after date I promise to pay to the order of State Bank Twelve Thousand Dollars at 10 Market Street, Harrisburg, Pennsylvania.

(signed)	Alvan Brill	(seal)
(signed)	Chester Davis	(seal)
(signed)	Eli Frame	(seal)
(signed)	George High	(seal)
(signed)	Ivan Jones	(seal)
(signed)	Ken Look	(seal)"

Upon inquiry, you find that the money had been borrowed from State Bank by the six individuals for a joint venture and that when the note fell due Alvan Brill paid the note on the demand of the bank. He has never received any contribution from the other makers. Your investigation further discloses that:

Chester Davis died December 1, 1945, and the First and Final Account of his Executors has been confirmed and distribution made.

Eli Frame was adjudicated a bankrupt on September 1, 1946, and thereafter discharged, but the note was not listed in the schedule of his liabilities.

George High, who is a financially responsible person, moved to California and presently resides there.

Ivan Jones, who is a financially responsible person, was a minor when the note was signed but became twenty-one years of age on December 1, 1947.

Ken Look, who likewise is a financially responsible person, still resides in Harrisburg.

What rights, if any, does Alvin Brill have against (1) Chester Davis' executors, (2) Eli Frame, (3) George High, (4) Ivan Jones, (5) Ken Look, and what amounts, if any, can he recover from *each* of the named parties? Explain.

QUESTION NO. VIII — WEIGHT: 10 POINTS

1. Could Pennsylvania enact and enforce laws defining bankruptcy and prescribing the administration of bankrupt estates? Explain.
2. Where a tenant is adjudicated a bankrupt, what is the maximum period of time for which the landlord has a preferred claim for unpaid rent?
3. Where goods of a tenant located upon the landlord's premises are levied upon by another creditor of the tenant, under the State Law what is the maximum period of time for which the landlord has a preferred claim for unpaid rent?
4. Of which of the following claims is a bankrupt *not* discharged?
 - a. Real estate taxes due a city
 - b. Damages for negligence
 - c. Damages for wilful and malicious injuries
 - d. Rent for bankrupt's home
5. Where an individual institutes a proceeding to be adjudicated a voluntary bankrupt and within three months of his adjudication inherits property, in whom does the title to such property vest?

QUESTION NO. IX — WEIGHT: 5 POINTS

1. Albert Bell purchased a car from Clarence Doyle and received a certificate of title therefor which appears to be regular on its face. Albert Bell insured the car with Universal Insurance Company for collision. The policy contained a representation of "sole ownership." While the car was parked, it was damaged due to the sole negligence of Earl Fohl. Thereafter, it was discovered that the car belonged to Guy Hill, having been stolen from him, and that the certificate of title was a forgery.
Does Albert Bell have a cause of action against (a) the Universal Insurance Company and (b) Earl Fohl? Explain.
2. If preferred stock in a Pennsylvania business corporation is issued with a fixed annual dividend but without any mention of whether or not the dividends are cumulative, are dividends on such stock cumulative or non-cumulative?
3. A plan for the reorganization of an insolvent corporation must be submitted to the Securities and Exchange Commission when the indebtedness of the corporation exceeds what amount?

4. How may a will, which has been lost, be cancelled by the maker?
5. Where a firm of certified public accountants are employed to make an audit, do the working papers, in the absence of an agreement relating thereto, belong to (a) the client, (b) the accounting firm, or (c) the employe of the firm who prepared the papers?

QUESTION NO. X—WEIGHT: 15 POINTS

You have been requested by the attorney for Commonwealth Bank, executor of Andrew Bigg's estate, to assist in the preparation of the following:

- a. Return showing property subject to four mill county tax.
- b. Schedule showing assets subject to Pennsylvania Transfer Inheritance Tax.
- c. Schedule showing assets subject to Federal Estate Tax.
- d. Schedule of assets with which the executor should charge itself when filing its First and Final Account.

Your investigation discloses that Andrew Biggs died on January 1, 1947, survived by a widow and son and that his gross estate exceeds \$100,000.00. In preparing the four reports above named you have been specifically requested to identify which of the following items owned by the decedent, unless otherwise indicated, should be entered in *each* of the reports:

1. \$10,000.00 in cash.
2. Shares of stock in a Delaware corporation which corporation is not registered in Pennsylvania and upon whose shares the corporation is not liable to tax in Pennsylvania.
3. Savings account in a state bank located in Pennsylvania.
4. Undivided one-half interest in real estate located in New York and owned by decedent and his brother as tenants in common. (Not sold by executor because devised to wife.)
5. Stock of a Pennsylvania business corporation now registered in the name of the son and given to the son on June 1, 1946, by decedent in contemplation of death.
6. Mortgage executed by a resident of Pennsylvania upon New York real estate. Interest on the mortgage is in default for two years.
7. Judgment against a Pennsylvania business corporation.
8. \$10,000.00 in a checking account deposited to the credit of the decedent and his wife as tenants by the entireties. This money was so deposited on September 1, 1946, from decedent's own funds and in contemplation of his death.
9. A 25% interest in a Pennsylvania partnership owning only real estate located in Pennsylvania.
10. \$1,000.00 collected on April 1, 1947, for royalties accruing between January 1, 1946, and January 1, 1947, on book written by decedent.
11. Insurance on the life of decedent purchased and paid for by him and made payable to his estate.

PENNSYLVANIA DEPARTMENT OF PUBLIC INSTRUCTION

12. Participation Certificate in a mortgage upon Pennsylvania real estate the legal title of which mortgage is vested in a Pennsylvania trustee.
13. Real estate located in Pennsylvania, the legal title to which was vested in the decedent and his wife as tenants by the entireties having been purchased wholly from funds of the wife.
14. Insurance on the life of decedent purchased and paid for by him and made payable to his wife.
15. Shares of stock of a national bank located in Pennsylvania and organized under the National Banking Laws.
16. Bond of a Pennsylvania third class city acquired by bequest from mother, who died on January 1, 1943, and upon which bond Pennsylvania Transfer Inheritance and Federal Estate Taxes were paid, by the mother's estate, based upon the valuation of the bond as of January 1, 1943. The value of the bond was the same on January 1, 1947, as it was on January 1, 1943.

Answer by placing a circle around the corresponding numbers appearing on the next page of this examination as illustrated by No. 1. If you believe explanations are necessary, place same on a separate sheet of paper.

Candidate No.

INSTRUCTION TO CANDIDATE

Insert your number at top of page. Detach the page from the examination question and securely fasten it to your answers. Use of pencil permitted.

County Tax Return	Assets Subject to Pennsylvania Transfer Inheritance Tax	Federal Estate Return	Schedule of Assets for Account
1	①	①	①
2	2	2	2
3	3	3	3
4	4	4	4
5	5	5	5
6	6	6	6
7	7	7	7
8	8	8	8
9	9	9	9
10	10	10	10
11	11	11	11
12	12	12	12
13	13	13	13
14	14	14	14
15	15	15	15
16	16	16	16